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IN THE
Supreme Court of the United States

October Term, 1943

No. 425

WILLIAM K. JACOBS, JR.,

Petitioner,

vs.

JANE M. HOEY, as executrix of the Estate of
James J. Hoey, Deceased,

Respondent.

**PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE SECOND CIRCUIT AND BRIEF IN
SUPPORT THEREOF**

DAVID L. SPRUNG,

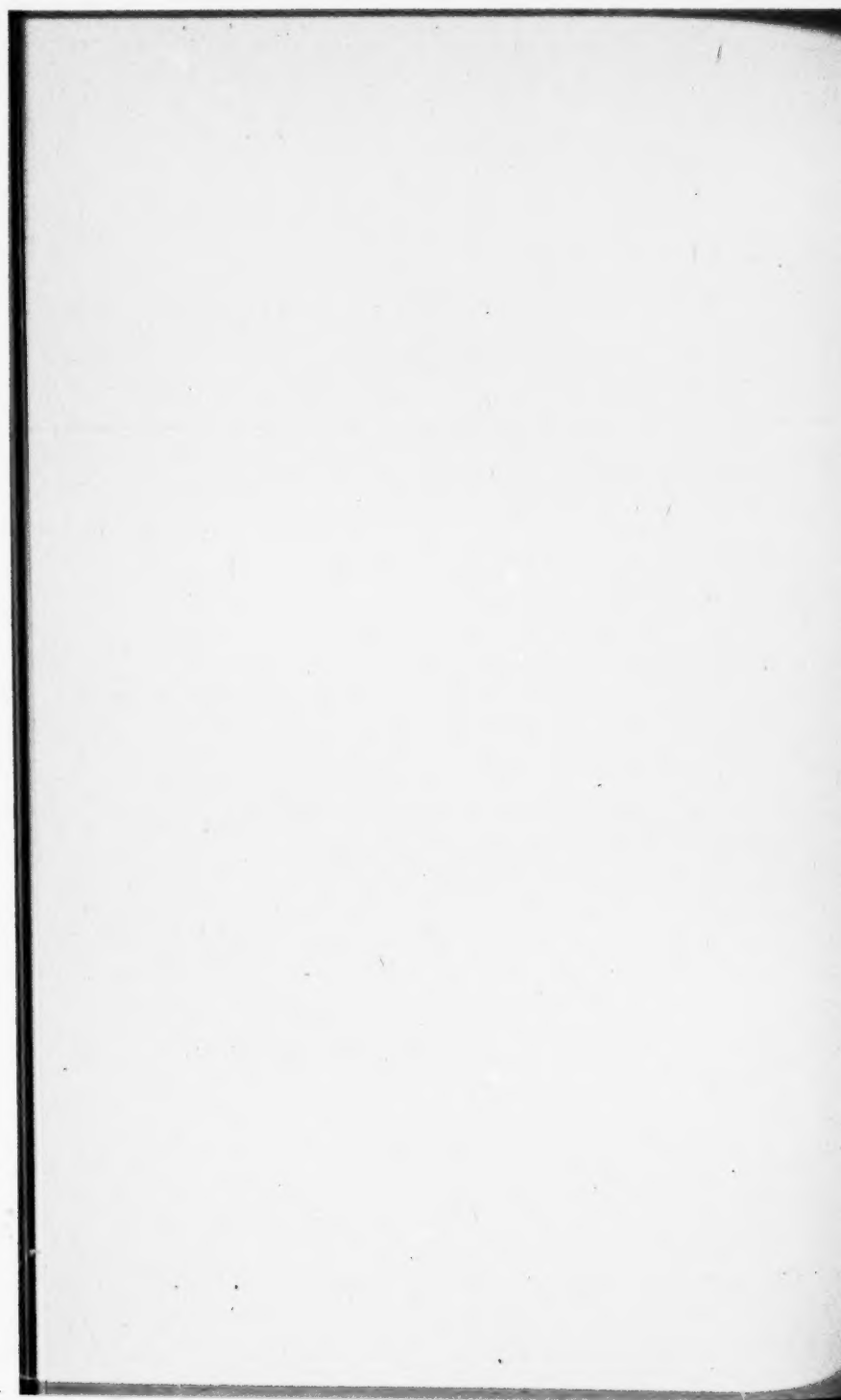
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No.

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Petitioner,

vs.

JANE M. HOEY, as executrix of the Estate of JAMES J. HOEY,
Deceased,

Respondent.

**PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE SECOND CIRCUIT AND BRIEF IN
SUPPORT THEREOF**

Petition

To the Honorable, the Chief Justice, and the Associate Justices of the Supreme Court of the United States:

The petitioner, William K. Jacobs, Jr., by his attorney, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered in the above cause on July 16, 1943, affirming the decision of the United States District Court for the Southern District of New York.

Summary Statement of Matter Involved

This action was brought in the United States District Court for the Southern District of New York for the refund of \$17,023.93 representing overpayment of income taxes for the years 1936 and 1937. Plaintiff, one of the five executors of the estate of Aaron E. Norman, deceased, requested and received from said estate on account of executor's commissions, advances of \$20,000 in 1936 and \$19,500 in 1937. Plaintiff included said sums in his income tax returns for said years and now contends that as a result thereof he overpaid taxes to the extent of \$9,835.74 in 1936 and \$7,188.19 in 1937. The Surrogate of New York County, having jurisdiction of the estate, did not approve the executors' accounts or authorize payment of their commissions until 1938.

Trial was had without a jury on November 12 and 13, 1942 before Judge Vincent L. Leibell. Judgment for defendant was entered on February 4, 1943 (R. 240). An appeal to the Circuit Court of Appeals for the Second Circuit was taken on February 4, 1943 (R. 242). The cause was argued on May 21, 1943 and on June 30, 1943, a decision was handed down whereby the judgment of the District Court was affirmed (R. 246). Judgment was entered on July 16, 1943 (R. 251).

Opinions Below

The opinion of the United States District Court for the Southern District of New York (R. 219) is unreported. The opinion of the Circuit Court of Appeals for the Second Circuit (R. 246) written by Judge Augustus N. Hand is reported at 136 F. (2d) 954.

Jurisdiction

The judgment of the Circuit Court of Appeals was entered on July 16, 1943 (R. 251). The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended (28 U. S. C. A. §347[a]).

The Question Involved

Whether for Federal Income Tax purposes, payments advanced to an executor on account of commissions are taxable in the year of receipt, or in the year in which the commissions are finally approved by the Surrogate having jurisdiction over the estate where under pertinent local law no commissions can legally be taken until such approval.

Statutes Involved

The applicable statutes, Sections 22 and 42 of Title 26, U. S. C. A. and Section 285 of the Surrogate's Court Act of New York insofar as relevant are set forth in the appendix.

Statement of Facts

The plaintiff alone testified, and offered numerous corroborating documents as exhibits. Defendant called no witnesses.

The relevant testimony and exhibits disclose that the will and codicils of Aaron E. Norman, deceased (Ex. N,*

* When an exhibit is referred to, the first reference indicates the page at which it was offered in evidence, the second reference indicates the page at which the exhibit appears.

R. 14, 114-130) were duly admitted to probate in the Surrogate's Court of New York County on August 3, 1936 (Ex. O, R. 14, 131). The will divided a gross estate in excess of \$3,000,000 (Ex. R, R. 32, 140; Finding of Fact 3, R. 229) among a number of beneficiaries. There were several small bequests, a large bequest of \$1,000,000 (Ex. R, R. 32, 147-151) and the creation of equal life interests in the residuary for the benefit of decedent's son and daughter. The remaindermen of these life interests were the daughter's three infant children and the son's two infant children (Ex. R, R. 32, 149-151; Finding of Fact 5, R. 230).

The plaintiff and four others named as executors, qualified on August 3, 1936 and entered upon their duties (R. 14; Finding of Fact 4, R. 229). The estate did not advertise for the presentation of creditors' claims (R. 14). On December 17, 1936, the executors executed an agreement in writing whereby three of them waived their rights to commissions, and the plaintiff and one other were to receive as commission a fixed percentage. This agreement by its terms was executed subject to approval of the Surrogate (Ex. P, R. 15, 132; Finding of Fact 6, R. 230). However, same was not submitted to the Surrogate for approval until the executors' account was filed in the Fall of 1938 (Finding of Fact 43, R. 237).

Shortly after the execution of this agreement, plaintiff requested the other executors for an advance on account of commissions (R. 16). The attorneys for the estate advised the executors that such advances, while illegal, were common (R. 18). Plaintiff thereupon orally agreed to indemnify and hold the other executors harmless from any liability that might arise by virtue of such an advance

(R. 18-19; Finding of Fact 7, R. 231). On December 23, 1936, plaintiff received from the estate an advance on account of executors' commissions in the sum of \$20,000 (R. 19; Ex. B, R. 19, 109).

In December of 1937, plaintiff again requested an advance and again made an oral agreement of indemnification, whereupon he received a further net advance of \$19,500 (R. 24, 26).

None of the parties interested in the estate except the other executors had been apprised of these advances. At the time of receiving these payments, the administration of the estate was in its early stages: The specific bequest of \$1,000,000 had not been paid (R. 21), the trusts had not yet been set up (R. 21), the estate tax had not been discharged (R. 21, 26-27), the guardians of the infant remaindermen had not been appointed (R. 21), and all creditors' claims had not yet been adjusted (R. 27). The Surrogate had not made the direction of the manner in which the value of real or personal property was to be determined; had not been apprised of the executors' agreement as to their compensation and had not determined the question of apportioning commissions among the executors (Findings of Fact 14, 31, 32, R. 232, 234, 235).

By advice of counsel embodied in a letter dated March 4, 1937 (Ex. W, R. 22, 177-9), plaintiff included the 1936 advance as part of his gross income and paid a tax thereon (R. 23; Ex. E, R. 23, 103; Finding of Fact 21, R. 233). On the same advice he did likewise with respect to the advance received in 1937 (R. 28; Ex. F, R. 29, 103; Finding of Fact 21, R. 233). Also, on advice of counsel (Ex. W, R. 22, 177-9) plaintiff made timely requests for refunds (R. 29; Ex. J, R. 30, 105; Finding of Fact 29, R. 234; Ex. K, R. 30, 106;

Finding of Fact 30, R. 234). These refund claims were rejected by the Internal Revenue Department (Ex. J-1, R. 30, 113; Ex. T, R. 31, 172).

On November 4, 1938, the executors filed an intermediate account (Finding of Fact 34, R. 235) and therein for the first time directed the Surrogate's attention to the earlier agreement on commissions (Finding of Fact 43, R. 237). This account was occasioned by the need for disposing of a number of minor problems and of obtaining a determination in respect to a disputed claim of \$700,000 against the estate (R. 31, Finding of Fact 35, R. 235) which the executors had every reason to believe would be litigated (Finding of Fact 40, R. 236). Immediately prior to the entry of the decree approving the account, the estate was relieved of this liability through a settlement, the financial burden of which was shouldered by others (R. 33; Finding of Fact 40, R. 236). On December 27, 1938, the Surrogate's decree approving the account and awarding the commissions was entered (Ex. Q, R. 34, 133).

On March 15, 1939, plaintiff filed his income tax return for the year 1938 (R. 46; Ex. G, R. 46, 104; Finding of Fact 46, R. 238) and explained therein that the Court had allowed him commissions of \$40,278.57 in the year 1938, but that inasmuch as he had paid taxes on a substantial part in the years 1936 and 1937, and his application for refund of said taxes had been rejected, that he had not included said commissions in the 1938 return although he believes same properly includible therein (Ex. G, R. 46, 104). Thereafter, plaintiff received a notice for a deficiency for the year 1938 upon the theory that taxes were payable on all of the commissions in the year when the final account thereof was fixed by the Surrogate (Ex. U, R. 48, 173; Finding of Fact 47, R. 238). Litigation in regard to this

deficiency assessment is presently pending before the United States Board of Tax Appeals (R. 49; Ex. AA, R. 49, 186; Ex. BB, R. 49, 192; Finding of Fact 48, R. 238).

These are the essential facts showing the circumstances under which the advances were made in 1936 and 1937, the need for an accounting in 1938, the judicial approval of the executors' commissions in 1938, and the precipitation of the question here presented as to whether such advances were part of gross income in the years when they were received.

Specification of Errors to be Urged

The Circuit Court erred:

1. In holding that the commissions advanced to the petitioner in 1936 and 1937 were income to him in those years, rather than in 1938 when the Surrogate approved these commissions.
2. In erroneously applying the "claim of right" doctrine in the *North American Oil* case* to payments made when there was neither the right to demand nor the duty to make such payments.
3. In not looking to the laws of the State of New York to determine the character of the commissions received in advance of Surrogate's approval.

Reasons for Granting the Writ of Certiorari

1. The decision of the Circuit Court below is in direct conflict with the decision of the Circuit Court of Appeals

* *North American Oil Consolidated v. Burnet*, 286 U. S. 417, 423, 424, 52 S. Ct. 613, 76 L. Ed. 1197.

for the Third Circuit in *Commissioner v. Cadwalader*, 88 F. (2d) 274; certiorari denied 301 U. S. 706. In the *Cadwalader* case the Third Circuit expressly held that in the State of New Jersey, where as in New York, executors are not entitled to commissions until the executors file their account and the commissions are allowed by the Orphans' Court, the executrices were taxable on commissions in the year when they were allowed by the Orphans' Court, although such commissions had been advanced to them in a prior year. The Court below in the instant case takes the opposite view—holding the advance commissions taxable in the year of receipt.

2. This case presents an important question on Federal Tax law of general interest to many taxpayers and to the Commissioner of Internal Revenue. The question has not been, but should be, definitely settled by this Court. By the multitude of cases in numerous states raising the issue of the propriety of an executor's taking commissions in advance of court approval, it is apparent that this practice is quite popular. It should, therefore, be finally determined when such commissions are taxable.

3. As a correlative to point "2" this Court should determine whether the Federal Courts are bound by decisions of the State Court holding such advances illegal under state legislation.

4. The Circuit Court below erroneously applied the "claim of right" doctrine set forth in *North American Oil Consolidated v. Burnet*, 286 U. S. 417, 423, 424, 52 S. Ct. 613, 76 L. Ed. 1197.

The doctrine is embodied in the opinion by Mr. Justice Brandeis which states in part:

"If a taxpayer receives earnings under a claim of right and without restriction as to its disposition he has received income which he is required to return, even though it may still be claimed that he is not entitled to retain the money, and even though he may still be adjudged liable to restore its equivalent."

A review of the facts in the *Burnet* case indicates exactly what this doctrine means. The Oil Company had operated certain land and the United States Government under a claim of title had instituted suit to oust the Company from possession. A receiver was appointed. He operated the land and derived substantial profits therefrom during the year 1916. In 1917, the suit was decided in favor of the Oil Company, the receiver was discharged and the profits turned over to the Oil Company. The Government took an appeal to the Circuit Court of Appeals. In 1920, that Court affirmed the decree and in 1922 a further appeal to the Supreme Court was dismissed by stipulation.

The question before the Supreme Court was in what year were the profits taxable to the Oil Company. The Supreme Court held that such money was not income in 1916 because "at no time during that year was there a right in the company to demand that the receiver pay over the money", that it was not income in 1922, the year in which the ownership litigation was finally terminated, but that it "became income of the company in 1917, when it first became entitled to them and when it actually received them."

This latter quotation precisely indicates what is meant when one receives money under a "claim of right". Note the word "and". A taxpayer cannot be said to have received money under a "claim of right" merely because he has received the money, he must also be legally entitled to receive the money. It should also be noted that in the *Burnet* case the duty to pay the money to the company, which made the Company entitled to receive it, was established by legal adjudication in its favor.

The Supreme Court has given to the words "claim of right" a definite legal connotation. They cannot be loosely applied to any circumstances where money is simply requested and received, nor interpreted to mean any claim short of larcenous. Payment under "claim of right" refers to a receipt when the recipient had a right to demand payment and when the paying party was under a duty to pay.

The Circuit Court below misapplied the doctrine to include receipt of payment when there was no right to demand nor duty to pay.

The New York law is well settled that under Section 285 of the Surrogate Court Act the right of an executor to commissions depends not only upon the rendition of the services, but also upon the settlement of the account. Until both events have occurred, the executor is not legally entitled to commissions (*Oakeshott v. Smith*, 104 App. Div. 284; aff'd 185 N. Y. 583, 78 N. E. 1108; *Beard v. Beard*, 140 N. Y. 260, 35 N. E. 488; *In re Bates' Estate*, 167 Misc. 641).

Hence, by deciding that the petitioner in the instant case when he took his commissions before the settlement of the estate accounting took under claim of right, the Circuit Court extended the doctrine of the *Burnet* case to an un contemplated degree.

First, it changed the determination of whether the taxpayer was entitled to the money when he received it from a question of law upon receipt to a question of fact to be resolved in the light of subsequent events. In the instant case, petitioner was not entitled to the advances in 1936 and 1937 because the legal adjudication namely, the Surrogate's award of commissions was lacking. In point of fact there existed numerous possibilities that the Surrogate might not award the commissions already advanced, be it for misfeasance, malfeasance, neglect the death of the executor, the non-approval by the Surrogate of the agreement as to the appropriation of fees, or for a host of other reasons (R. 21, 26, 27). It was only in 1938 upon the handing down of the decree by the Surrogate was it first determined that petitioner was entitled to the commissions. Until then the advances were mere loans. (*In re Julia's Estate*, 3 N. J. Misc. 976; 130 A. 733, 735.)

Second, the Court below added degrees of legality or rather of illegality to the doctrine, additions never intended by the Supreme Court. The *Burnet* case succinctly stated that the money became income when the Company "first became entitled to them and when it actually received them." Therefore, a taxpayer in order to take under a claim of right must have been entitled to receive the money. The word "entitled" means what it says—the legal right to receive. The Circuit Court below mistakenly held the receipts in question as payments under a "claim of right" because no fraud was involved—though it was definitely illegal—and because by hind sight it would appear that no serious doubt existed that the Surrogate would ultimately decree payment of commission exceeding the amounts improperly advanced.

The controlling factor herein is that plaintiff did not have the right to demand and the estate did not have the duty to pay advances of commissions in 1936 and 1937. It is, therefore, contended that the moneys received by the plaintiff were not so received under a claim of right; they were not compensation for personal services within the meaning of Section 22 of the Revenue Act and were, therefore, not taxable income.

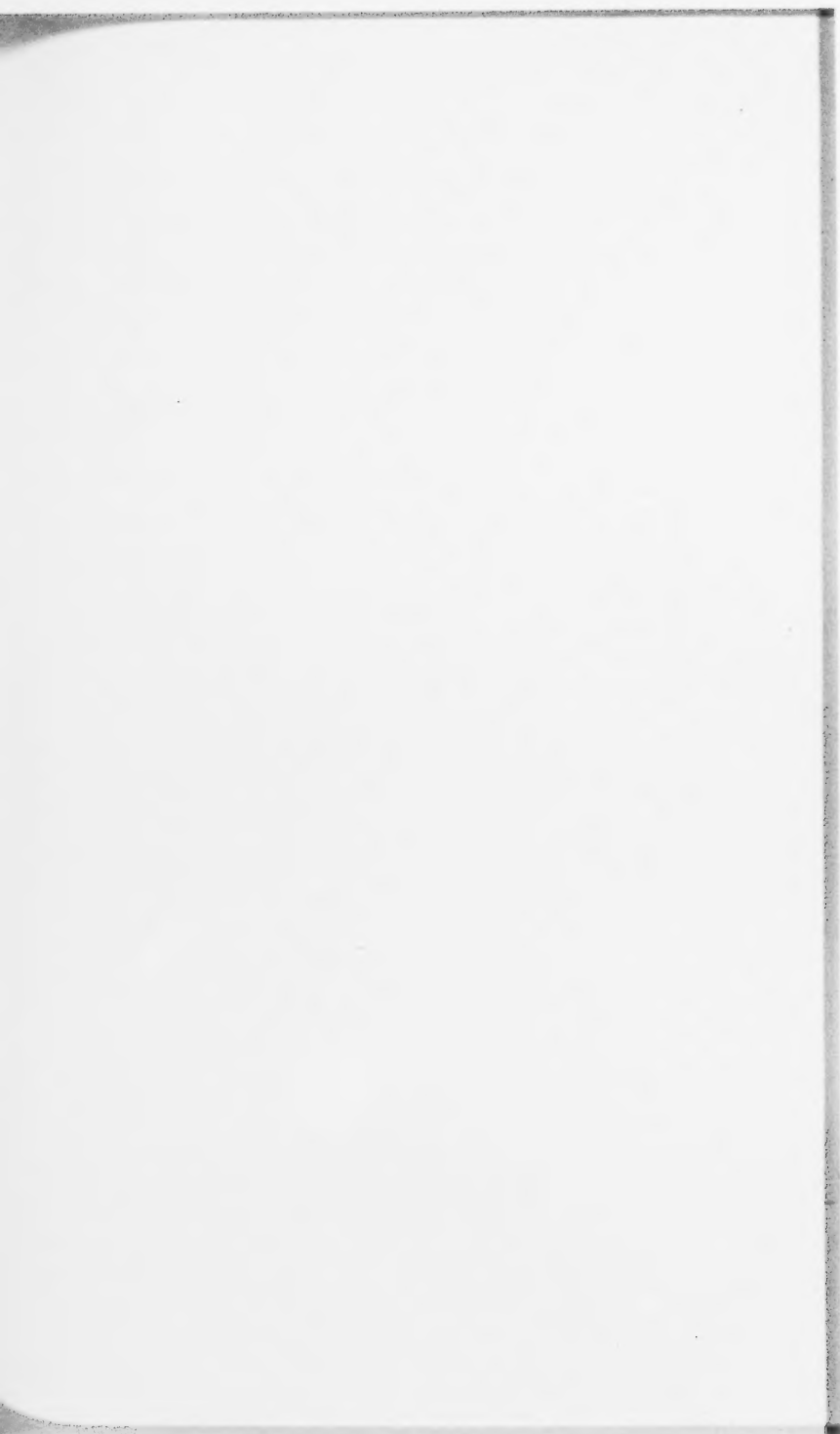
It is respectfully submitted that the points at issue should be decided by this Honorable Court.

WHEREFORE, it is prayed that this petition for a writ of certiorari be granted.

Respectfully submitted,

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BRIEF IN SUPPORT OF PETITION**ARGUMENT***Summary*

- POINT I. THE FEDERAL COURTS ARE BOUND BY THE NEW YORK LAW THAT THE ADVANCE OF MONIES TO AN EXECUTOR, PRIOR TO SURROGATE'S APPROVAL REQUIRED BY STATUTE, IS ILLEGAL AND THE TRANSACTION A MERE LOAN.
- POINT II. THE DECISION IN THE COURT BELOW IS IN CONFLICT WITH THE DECISION IN COMMISSIONER V. CADWALADER IN THE THIRD CIRCUIT AND WITH THAT OF THE SOLICITOR OF INTERNAL REVENUE.
- POINT III. THE DECISIONS CITED IN THE COURT BELOW ARE CLEARLY DISTINGUISHABLE FROM THE INSTANT CASE.

POINT I

The Federal Courts are bound by the New York Law that the advance of monies to an executor, prior to Surrogate's approval required by statute, is illegal and the transaction a mere loan.

The Norman estate was administered in the courts of the State of New York. Fixing and paying executor's compensation are governed by Section 285 of the New York Surrogate's Court Act. This statute and the decisions thereunder clearly establish that an advance to an executor

preceding the Surrogate's decree is illegal. Therefore, the payments made to plaintiff in 1936 and 1937 were surchargeable, and in legal effect mere loans, despite any contrary intention of the parties.

The pertinent provisions of Section 285 of the Surrogate's Court Act are:

"On the settlement of the account of any executor, * * * the Surrogate must allow to such executor, commissions, * * * for his services in such official capacity, and if there be more than one, apportion among them according to the services rendered by them respectively."

The courts have decided that the right of commissions under this and similar statutes depends upon the rendition of the service and the settlement of the account. Until both events have occurred, the executor is not legally entitled to commissions (*Oakeshott v. Smith*, 104 App. Div. 384; affd. 185 N. Y. 583, 78 N. E. 1108; *Beard v. Beard*, 140 N. Y. 260, 35 N. E. 488). Taking commissions in advance of the account is improper (*In re Bates' Estate*, 167 Misc. 641). Upon the making of such an advance payment, it is improper for an executor to set up credit in his accounts therefor (*In re Collins' Estate*, 158 Misc. 798). The monies so advanced are held to be the equivalent of cash on hand in the possession of the estate (*Matter of Dunkel, Jr.*, 10 N. Y. St. R. 213). Even in the absence of executing a note therefor, the executor receiving such an advance is liable to repay to the estate the amount thereof with interest (*Wheelwright v. Rhoades*, 28 Hun. 57). Under similar statutory provisions it was held that the executor taking such commissions in advance occupies the position of borrower of the amount so taken (*In re Jula's Estate*, 3 N. J.

Misc. 976; 130 A. 733, 735). Until the accounting, the right to commissions is inchoate (*Matter of Worthington*, 141 N. Y. 9, 35 N. E. 929), and cannot therefore be assigned (*In re Furness*, 75 F. [2d] 965; *Lockhart v. Mittlemann*, 123 F. [2d] 703).

The trial court concluded as a matter of law (Conclusion of Law III, R. 239) that the payments made to plaintiff in 1936 and 1937 were illegal. Therefore, it necessarily follows that plaintiff did not have the right to demand nor the estate the obligation to make those payments. The conclusion is equally inescapable that under the laws of the State of New York, the legal effect of the transaction was to make plaintiff a borrower, and not to compensate him for personal services.

Other New York cases emphasize the executor's risk in taking any advance since there are many contingencies which may reduce or even remove the right to commissions when the time for the accounting arrives. Thus the New York courts have determined that despite the use of the word "must" in the New York statute, the Surrogate nevertheless has the right in his discretion to deny or substantially reduce commissions for inattention to duty (*Matter of Rutledge*, 162 N. Y. 31, 56 N. E. 511; *In re Sharp's Estate*, 140 Misc. 427), or for neglect or unfaithfulness (*Stevens v. Melcher*, 152 N. Y. 551, 46 N. E. 965) or in the event of death (*Matter of Bushe*, 227 N. Y. 85, 129 N. E. 154) or resignation (*In re Douglas*, 60 App. Div. 64). It has been further held that the amount of commissions depends on the rate prevailing at the time of the accounting (*In re Barker*, 230 N. Y. 364, 372, 130 N. E. 579; *Estate of Henry Harris*, 1 N. Y. St. R. 331; *Lewis v. Bowers*, 19 F. Supp. 745). Further risks in premature appraisal of commissions to justify an advance were taken by petitioner

because of the provision (§285 [5], see appendix) that the value of real or personal property is to be determined in such manner as the Surrogate directs, and also the provision (§285 [8], see appendix) that where there are three executors the commissions are apportioned among them according to the services rendered by them respectively.

In the instant case the contingencies were real inasmuch as the plaintiff's commissions might have been disallowed completely or cut substantially if he had died, resigned, been guilty of misfeasance, malfeasance, neglect or inattention to duty; or if the rate of compensation had materially changed; or if the Surrogate had directed the valuation of the real or personal property in a manner different than that adopted by the executors; or if large specific legatees, the guardians of the remaindermen, or creditors of the estate had protested against the allowances or had demanded surcharge for the illegal taking thereof. Furthermore, in this case the executors had agreed in 1936 as to the apportionment of fees among themselves (Ex. P, R. 15, 132; Finding of Fact 6, R. 230). This was subject to Surrogate's approval. The Surrogate in 1938 might very well have refused to adopt this agreement as to commissions. The taxability of improper advances should not be conditioned by subsequent developments in the administration of the estate.

The Court below erred in discounting the New York decisions on the theory that hindsight revealed that the decree of 1938 granted commissions in excess of the earlier advances. Whether the advances of 1936 and 1937 are income in those years must be determined by the character of the transaction at the time of their receipt. The existing interpretation by State Courts of the pertinent State

Statutes apply in the Federal Courts. *Commissioner v. Cadwalader*, 88 F. (2) 274, cert. den. 301 U. S. 706; cf. *Helvering v. Stuart*, 317 U. S. 154, 63 S. Ct. 140, 87 L. Ed. 109; *Blair v. Commissioner*, 300 U. S. 5, 57, S. Ct. 330, 81 L. Ed. 465.

The court below erroneously disregarded decisions of the New York courts establishing that in 1936 and 1937 the petitioner had no right to receive these funds. The effect of the New York law on executor's commissions was a legal fact to be considered by the court in determining the ultimate Federal question—in what year were the commissions received as income within the meaning of the Revenue Act.

POINT II

The decision in the Court below is in conflict with the decision in *Commissioner v. Cadwalader*, in the Third Circuit and with that of the Solicitor of Internal Revenue.

By §42 of the Revenue Act of 1934 and subsequent acts (26 U. S. C. A. §42) all items of gross income must be included "for the taxable year in which received by the taxpayer * * *" but the question remains—what is "gross income?" This term is defined in §22 of the Revenue Act (26 U. S. C. A. §22) to include "compensation for personal services * * * of whatever kind and in whatever form paid * * *." The authorities establish that the receipt of money is not the sole test of taxability; in the case of executor's commissions advances on commissions are not part of the taxable income in the year of receipt.

Commissioner v. Cadwalader, 88 Fed. (2) 274, cert. denied 301 U. S. 706, is on all fours with the instant case.

It deals with an estate administered under the New Jersey laws. Section 129 of the Orphans' Court Act of New Jersey (3 N. J. Comp. St. 1910, p. 3860, §129), which provides that:

“ ‘The commissions of executors, * * * shall be determined by the Orphans' Court on the final settlement of their accounts * * * ’ ”

has been construed as has been Section 285 of the Surrogate's Court Act of New York. Under the New Jersey law, just as under the New York law, executors are not entitled to fees or commissions until the final account is filed and the fees and commissions are allowed by the Orphans' Court. (*In re Smith's Estate*, 107 N. J. Eq. 607, 153 A. 647; *Titsworth v. Titsworth*, 107 N. J. Eq. 436, 152 A. 869; *Wyckoff v. O'Neil*, 72 N. J. Eq. 880, 67 A. 32.)

Because of the unliquid position of the estate, cash was borrowed and turned over to the executrices as advances on their commissions. The question presented was also in what year were such advances taxable, when received or when finally approved.

The Board of Tax Appeals at 32 B. T. A. 1157 held that the advances were taxable in the year of receipt. On appeal to the Circuit Court of Appeals for the Third Circuit, that court reversed the holding of the Board, maintaining that the advances were not deemed to have been received and hence not taxable until the year of court approval.

In S. M. 1925, IV-I, C. B. 125 the same conclusion was reached by the Solicitor of Internal Revenue where a Maine statute (see appendix) similar to the New York statute was involved. Executor estimated his commissions and withdrew securities in that amount from the estate. He executed in favor of the estate a non-interest bearing

note for the amount, to be held by the estate until the commissions were authorized by the court. The Solicitor determined that until court approval the taxpayer had no legal right to any commissions and therefore none were earned in advance of such approval.

In both of the aforementioned cases, the State statute governing executors' commissions was similar to the New York statute involved herein. In both cases in contradistinction to the decision in the court below the law of the particular state was looked to, to determine the character of the advance commissions. Also in both cases since the state laws held the advances, taken without the legal right to demand nor to receive, to be mere loans, the conclusion was reached that the advance on commissions were not compensation and hence not taxable in the year of receipt, but only when finally approved by the court.

We submit, therefore, that in view of the fact that the decision in the instant case is directly in conflict with a decision in the Third Circuit and with a decision of the Internal Revenue Department, for the purposes of uniformity this court should grant certiorari herein to determine finally the principle of law in question.

POINT III

The decisions cited in the Court below are clearly distinguishable from the instant case.

The lower court in its opinion has cited numerous decisions in support of its conclusion. A review of these cases indicates such sharp differences between them and the instant case so as to render them impotent as authority for the conclusions invoked in the court below.

The case of *North American Oil Consolidated v. Burnet*, *supra*, cited by the court below at 136 F. (2d) 956 (R. 249) has been dealt with at length in the petition herein (pp. 8-12). There it was shown that the "claim of right" doctrine as set forth in that case cannot apply to the instant case, for the reason that petitioner in 1936 and 1937, when he received the advances on commissions, did not have the legal right to demand, and the estate the legal obligation to pay same.

The rest of the cases cited by the court below in its decision fall into three main categories and are all readily distinguishable from the instant case.

In *Board v. Commissioner*, 51 F. (2) 73 (C. C. A. 6th) cited by the court below at page 956 (R. 250); *Mitchell v. Commissioner*, 89 F. (2) 873 (C. C. A. 2d) cited by the court below at page 957 (R. 250); *Saunders v. Commissioner*, 101 F. (2d) 407 (C. C. A. 10th) cited by the court below at page 957 (R. 250); *Griffin v. Smith*, 101 F. (2d) 348 (C. C. A. 7th); cert. denied 308 U. S. 561 cited by the court below at page 957 (R. 250) the respective taxpayers all received the moneys in question under a "claim of right" just as in the *North American Oil* case, *supra*. In each case, at the time of receipt there was a legal right in the recipients to demand the money and/or a duty in the payors to pay the money, even though later the recipients might have had to return the money for varied reasons, at which time a proper loss deduction could be taken. In the instant case, however, the estate was not under a duty to pay on the dates it did so. Indeed the estate was under a duty not to pay and the petitioner did not have the legal right to demand the advances.

In *National City Bank of New York v. Helvering*, 98 F. (2) 93 (C. C. A. 2d) cited by the court below at pages 956-7

(R. 250-1) and in *Barker v. Magruder*, 95 F. (2) 122, 68 App. D. C. 78, cited by the court below at pages 956-7 (R. 250-1) the question was presented when illicit income should be reported. It was held in the first case where the taxpayer reported on the cash receipt basis that it be reported in the year of receipt and in the second case where the taxpayer reported on the accrual basis that it be reported in the year that the income accrued. This is sound reasoning. When else should a tortfeasor be taxed for illicit gains other than in the year of receipt or accrual as the case may be. The taking in such cases could never become legal so as to be taxable in the year of validation while in the instant case the advance though improper when taken was validated upon judicial decree on accounting.

In *United States v. S. S. White Dental Mfg. Co.*, 274 U. S. 398, 47 S. Ct. 598, 71 L. Ed. 120 cited by the court below at page 956 (R. 250) and in *Brown v. Helvering*, 291 U. S. 193, 199, 54 S. Ct. 356, 78 L. Ed. 725, cited by the court below at page 956 (R. 250) the question before the courts was whether certain deductions could properly be taken by the respective taxpayers in particular years. In the first case, the taxpayer, a corporation took a loss in 1918 when its property was sequestered by the German government. In 1922 some recovery was had reducing the loss reported. The court maintained that the possibility of recovery in 1918 was so negligible so as to justify the deduction taken.

In the instant case, however, the petitioner could not at all be sure that at a future date the Surrogate would approve the commissions he advanced himself. There existed too many uncertain contingencies which would have to be disposed of before final judicial approval (see p. 16, *supra*).

In the second case, an insurance agent accounting on the accrual basis wanted to deduct from the amount of commissions which he received on business written during the year, the amount which in view of past experience he anticipated he would be called upon to refund in future years on account of cancellations. The court refused to allow this deduction, holding that the contingencies did not affect the income quality of the commissions received since when received the "general agent's right to it was absolute." However, in the case at bar, the right of petitioner to the advances was far from absolute; in fact his receipt of the advances was illegal and improper and in effect but a loan.

It is evident, therefore, that though the decisions in the aforementioned cases are justifiable when viewed from the perspective of their respective facts, they can have no application to the instant case.

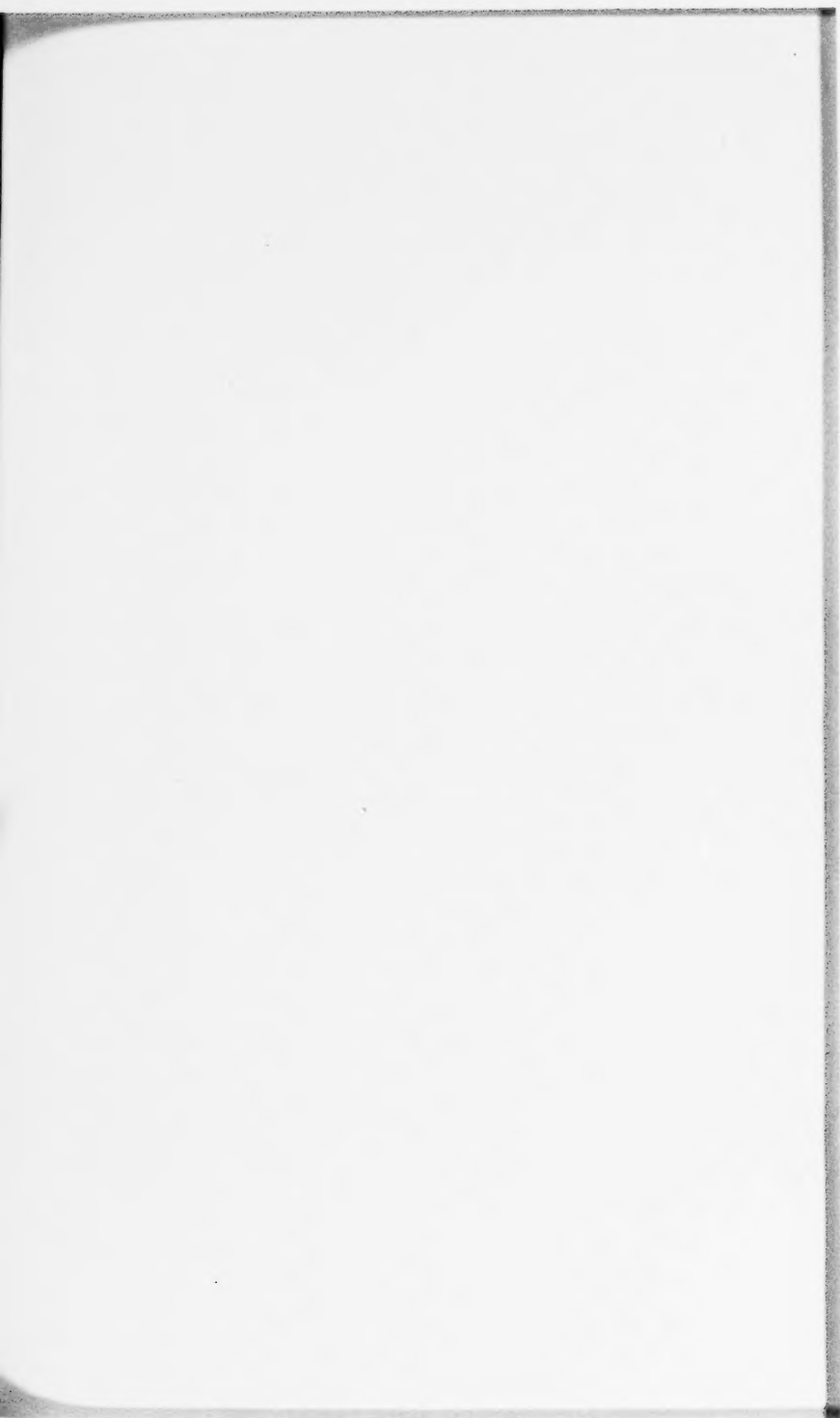
CONCLUSION

For the reasons heretofore assigned, it is respectfully submitted that the case is one which justifies the issuance of a writ of certiorari.

Respectfully submitted,

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Of Counsel.



APPENDIX

Title 26, U. S. C. A., Section 22, provides, in part, as follows:

“(a) General definition. ‘Gross income’ includes * * * compensation for personal service, * * * of whatever kind and in whatever form paid * * *.”

Title 26, U. S. C. A., Section 42, provides, in part, as follows:

“Section 42. Period in which items of gross income included. The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under Section 41, any such amounts are to be properly accounted for as of a different period. * * *”

New York Surrogate's Court Act, Section 285, provides, in part, as follows:

“SECTION 285. *Commissions of executor, administrator, guardian or testamentary trustee.* On the settlement of the account of any executor, administrator, guardian or testamentary trustee, the surrogate must allow to him his just, reasonable and necessary expenses actually paid by him, * * * and in addition thereto the surrogate must allow to such executor, administrator, guardian or testamentary trustee for his services in such official capacity, and if there be more than one, apportion among them according to the services rendered by them respectively.

1. For receiving and paying out all sums of money not exceeding two thousand dollars, at the rate of five per centum.

2. For receiving and paying out any additional sums not amounting to more than twenty thousand dollars, at the rate of two and one-half per centum.

3. For receiving and paying out any additional sums not exceeding twenty-eight thousand dollars, at the rate of one and one-half per centum.

4. For all sums above fifty thousand dollars, at the rate of two per centum.

5. The value of any real or personal property, to be determined in such manner as the surrogate may direct, and the increment thereof, received, distributed, or delivered, shall be considered as money in making computation of commissions. But this shall not apply in case of a specific legacy or device.

* * * *

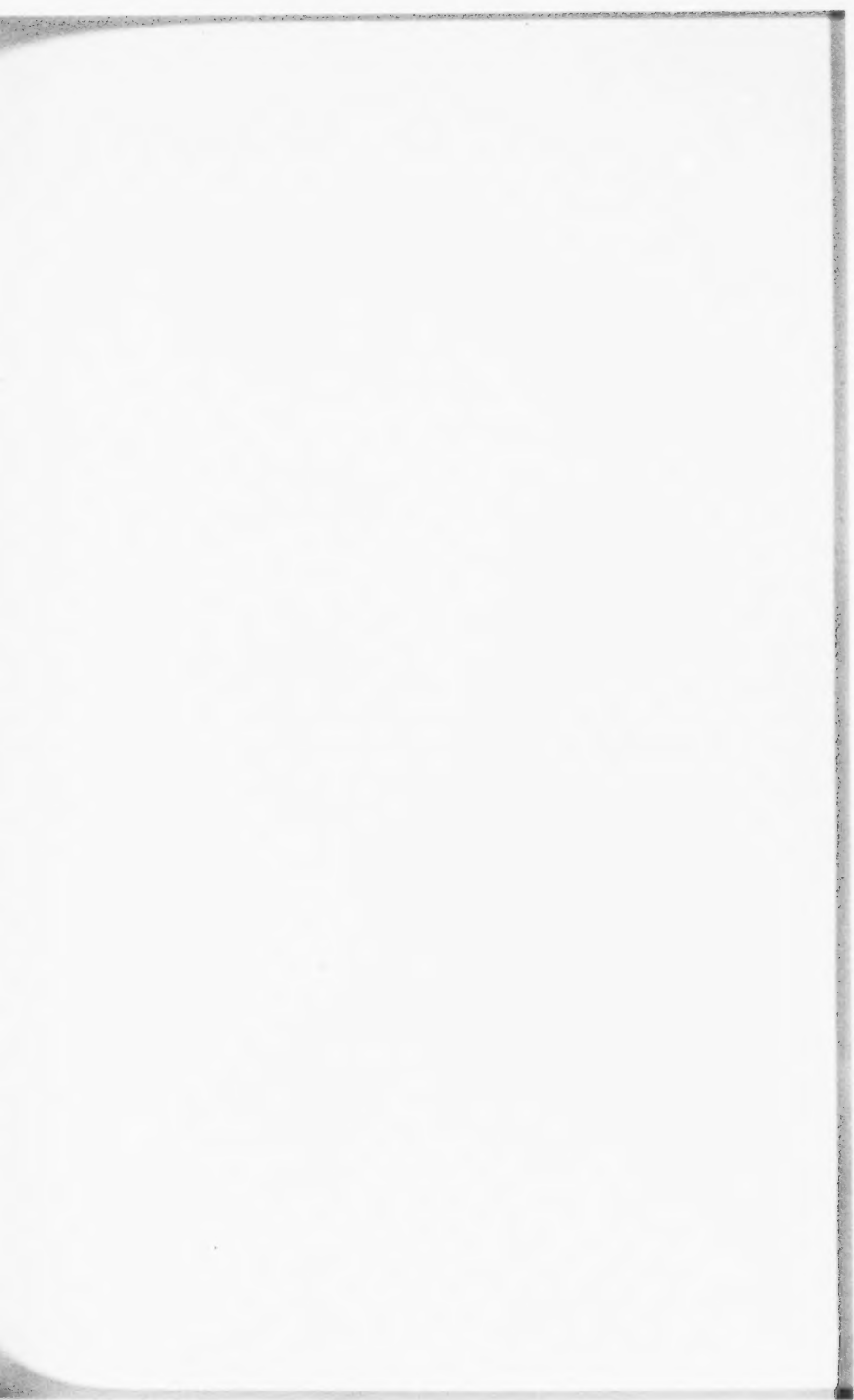
8. If the gross value of the principal of the estate or fund accounted for amounts to one hundred thousand dollars or more, each executor, administrator, guardian or testamentary trustee is entitled to the full compensation on principal and income allowed herein to a sole executor, administrator, guardian or testamentary trustee, unless there are more than three, in which case the compensation to which three would be entitled must be apportioned among them according to the services rendered by them, respectively. * * *

Orphans' Court Act of New Jersey, 3 N. J. Comp. St. 1910, p. 3860, Section 129, provides, in part, as follows:

“ ‘The commissions of executors, * * * shall be determined by the Orphans' Court on the final settlement of their accounts * * *.’ ”

Revised Statutes of Maine, Section 43, Chapter 67, Title 6, provides, in part, as follows:

“Executors * * * may be allowed * * * at the discretion of the judge, * * * a commission not exceeding five per cent on the amount of personal assets that come into their hands. * * *”



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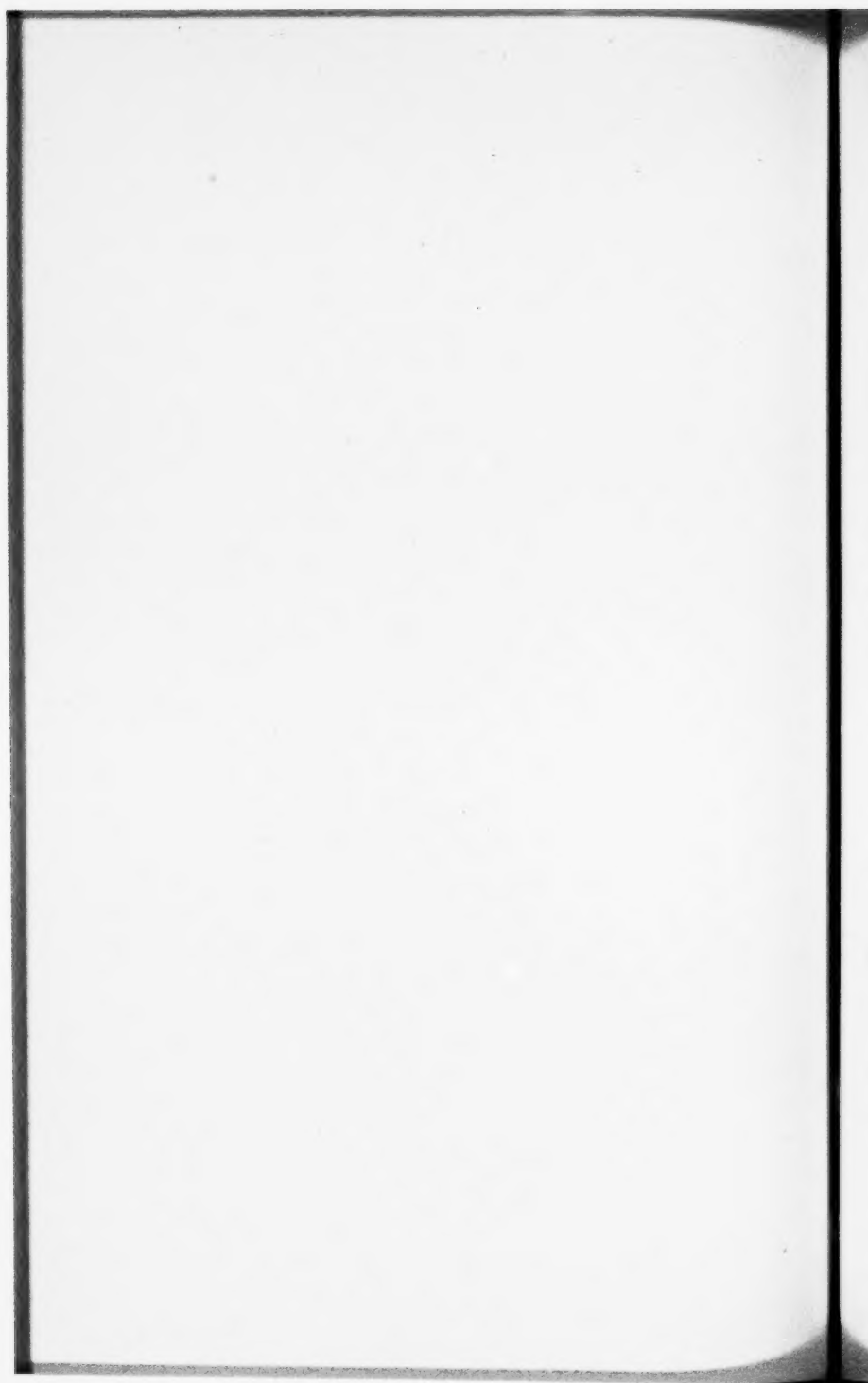
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(I)



In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 425

WILLIAM K. JACOBS, JR., PETITIONER

v.

JANE M. HOEY, AS EXECUTRIX OF THE ESTATE OF
JAMES J. HOEY, DECEASED

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED
STATES CIRCUIT COURT OF APPEALS FOR THE SECOND
CIRCUIT*

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 219-228) is unreported. The opinion of the Circuit Court of Appeals (R. 246-251) is reported in 136 F. 2d 954.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on July 16, 1943 (R. 251-252). The petition for a writ of certiorari was filed on October 15, 1943. The jurisdiction of this Court is

(1)

invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether petitioner, on the cash receipts basis, is required to include in gross income payments on account of executor's commissions in the year of receipt or in the later year when those payments were approved by the Surrogate.

STATUTES INVOLVED

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

SEC. 42. PERIOD IN WHICH ITEMS OF GROSS INCOME INCLUDED.

The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of account-

ing permitted under section 41, any such amounts are to be properly accounted for as of a different period. * * *

STATEMENT

The pertinent facts herein involved are as follows:

Aaron E. Norman died on July 1, 1936, leaving an estate having a gross value in excess of \$3,000,000. His will was admitted to probate by the Surrogate of New York County, and letters testamentary were issued on August 3, 1936, to the five executors named in the will (R. 229).

On December 17, 1936, the five executors agreed with one another in writing, subject to the approval of the Surrogate, that petitioner, one of the executors, would receive 2% as his commissions as executor, that John S. Borg, another of the executors, would receive 1½% as his commissions, and that the remaining three executors, who were members of the decedent's family, would waive their commissions (R. 230). Prior to December 23, 1936, petitioner, knowing that his commissions would amount to about \$60,000 if he properly performed his duties as executor, requested his coexecutors for a payment of \$20,000 on account of such commissions. His coexecutors agreed to the payment, subject to the approval of counsel. Petitioner was then advised by counsel for the executors that such advance on account of commissions, while irregular, was not infre-

quently made, and it had been held in a recent decision not to render the executor chargeable with interest where the estate had not been prejudiced. Accordingly, the other executors approved payment of \$20,000 to petitioner in 1936, and a further payment of \$19,500 in 1937, in consideration of his promise to indemnify them against any liability which might result therefrom. (R. 79-81, 220-221, 231.)

In connection with the payment on account of commissions made in 1937, counsel for the executors wrote a letter of advice to each of the executors which concluded thus (R. 180):

In summary, we wish to state that payment of commissions to Executors prior to an accounting is frequently done, and there is no illegality in making such payment. The only risk that is run is the risk that the Surrogate will not allow the statutory commissions, which disallowance occurs only in the event of negligent or dishonest performance of duties by the Executors.

When the executors had their first accounting in the year 1938, the Surrogate, by decree of December 27, 1938, allowed the sums taken as commissions in 1936 and 1937 without charging interest against the petitioner because the payments had been made in advance of a judicial settlement (R. 138, 227).

The petitioner commingled the payments he had received on account of commissions in 1936 and

1937 with his own funds, and treated them as payments of commissions both on his own books, and on the books of the estate; both sets of books were kept under his direction, and on the cash receipts basis. In his income tax returns for those years he included the payments as though they were executor's commissions earned at the time he received the advances, and in the returns for the estate he deducted as administration expenses that part of the commissions he had received which was attributable to income. (R. 228, 232-233.)

In 1938, the petitioner incurred a loss in the liquidation of the American Portraiture Corporation, of which he was owner. This capital loss he would have been able to offset against the commissions he had received in 1936 and 1937 if they were properly attributable to the year 1938 in which they were allowed by the Surrogate. (R. 224.) He had been advised by counsel that there was reason to believe that the tax authorities would insist that the payments on account of commissions ought to have been made during the year 1938, when they were formally allowed by the Surrogate, rather than in the years when they were taken. With reference to such payments, counsel advised the petitioner that, if the taxing authorities should claim that they ought to have been included in the return for 1938 income, any overpayment of taxes that had been assessed on the sums received as commissions during the prior

years could be cured either by filing amended returns, or by bringing an action for refund. (R. 222.)

Petitioner never disclosed to the Collector or the Bureau of Internal Revenue that the Surrogate had not approved the commissions at the time when they were paid until about May 1938, by which time it was clear that the petitioner would have a large capital loss to offset, either in whole or in part, any income from commissions which could properly be allocated to the year 1938 (R. 234).

The petitioner filed claims for refunds of the taxes that had been assessed against him on the receipt of commissions in 1936 and 1937, which he had included in his returns of income for those years (R. 234). Upon the rejection of the refund claims by the Commissioner, the petitioner brought suit to recover \$9,835.74 alleged to have been unlawfully collected because of the \$20,000 he had received from the Norman estate in 1936, and \$7,188.19 alleged to have been unlawfully collected because of the \$19,500 he had received in 1937 (R. 3-8). The District Court dismissed the complaint upon the ground that the payments made in 1936 and 1937 on account of commissions were received by petitioner under a claim of right and without restriction as to their disposition and, therefore, constituted taxable income for the

years of their receipt (R. 219-241). The Circuit Court of Appeals affirmed the decision of the District Court (R. 246-251).

ARGUMENT

The court below correctly concluded that the payments received by petitioner in 1936 and 1937 on account of commissions were income for the years of receipt and taxable as such for those years. "No rule is better established in tax law" (*Barker v. Magruder*, 95 F. 2d 122, 124 (App. D. C.)) than that "If a taxpayer receives earnings under a claim of right and without restriction as to its disposition, he has received income which he is required to return, even though it may still be claimed that he is not entitled to retain the money, and even though he may still be adjudged liable to restore its equivalent." *North American Oil v. Burnet*, 286 U. S. 417, 424. Since the assessment of federal income taxes is on the basis of an annual accounting period (*Burnet v. Sanford & Brooks Co.*, 282 U. S. 359), no other doctrine is practically possible. See *National City Bank of New York v. Helvering*, 98 F. 2d 93 (C. C. A. 2d). The decisions are, therefore, virtually unanimous in holding that a taxpayer is chargeable with taxable income in the year of receipt notwithstanding infirmities of title and the possibility of being compelled to respond to others for the amounts received. See *Chicago*,

R. I. & P. Ry. Co. v. Commissioner, 47 F. 2d 990 (C. C. A. 7th); *Board v. Commissioner*, 51 F. 2d 73 (C. A. A. 6th), certiorari denied, 284 U. S. 658; *Ford v. Commissioner*, 51 F. 2d 206 (C. C. A. 6th), certiorari denied, 284 U. S. 666; *Blum v. Helvering*, 74 F. 2d 482 (App. D. C.); *Mitchell v. Commissioner*, 89 F. 2d 873 (C. C. A. 2d); *Barker v. Magruder*, *supra*; *National City Bank of New York v. Helvering*, *supra*. And that rule has been applied even where the taxpayer has in fact restored in a subsequent year the amount previously received. *Griffin v. Smith*, 101 F. 2d 348 (C. C. A. 7th), certiorari denied, 308 U. S. 561; *Saunders v. Commissioner*, 101 F. 2d 407 (C. C. A. 10th).

In the instant case the District Court was justified in finding as a fact that petitioner received the amounts in question under a claim of right and without any restriction as to their disposition. (R. 232.) Those amounts were paid to him upon advice of counsel to the effect that payments of commissions to executors prior to final accounting were frequently made, and that the only risk involved would be disallowance of those commissions by the Surrogate in the event of negligent or dishonest performance of duties by the executors. See *Beard v. Beard*, 140 N. Y. 260. The payments were received with the permission of petitioner's coexecutors and members of the decedent's family who were chiefly interested in the estate. There was, therefore, no reasonable like-

lihood that petitioner would be called upon to return the sums paid to him; nor was he in fact required to do so. Moreover, the petitioner deposited the sums received with his other personal income and used those funds for his own personal purposes. His own books and the estate's books recorded the amounts received as commission payments earned.

We submit, therefore, that even if it be said that payment of the commissions to petitioner in 1936 and 1937 was technically improper, he clearly received them under a claim of right and without restriction as to their disposition.¹ His conduct unequivocally so indicates; and neither he nor any other person has ever questioned his claim. On the contrary, the Surrogate, by decree of December 27, 1938, actually approved the payments.

Commissioner v. Cadwalader, 88 F. 2d. 274 (C. C. A. 3d), certiorari denied, 301 U. S. 706, is not in conflict with the instant case. In the *Cadwalader* case, the estate being without funds with which to pay executor's commissions, the executrix in 1925 advanced money to herself and

¹ Despite petitioner's assertion (Br. 11) that "a taxpayer in order to take under a claim of right must have been entitled to receive the money," the decided cases make it clear that it is necessary at most that the taxpayer merely *claim* to be entitled to the money, not that he *in fact* be entitled to it. See *Griffin v. Smith*, *supra*; *Saunders v. Commissioner*, *supra*; *Ford v. Commissioner*, *supra*; *Barker v. Magruder*, *supra*; *National City Bank of New York v. Helvering*, *supra*.

issued a note to herself covering the so-called loan. She immediately took back the money, together with the note. The decision of the court was rested on the ground that she had properly omitted such amount from her taxable income in 1925 since she had received no income from the estate that year, but "had in effect simply received a note for her claimed commission and the whole matter was one of accommodation in order that the * * * estate might secure a deduction for tax purposes" (p. 275).

CONCLUSION

The decision of the court below is correct. It presents no conflict or question which would warrant further review. We respectfully submit that the petition should be denied.

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SAMUEL O. CLARK, Jr.,
Assistant Attorney General.

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Special Assistants to the Attorney General.

NOVEMBER 1943.

